

Message Text

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AMEMBASSY GUATEMALA

C O N F I D E N T I A L SECTION 1 OF 2 PANAMA 8521

GUATEMALA FOR ROCAP

E.O. 11652: GDS
TAGS: ECON, EFIN, PN
SUBJECT: PANAMA'S ECONOMY CONTINUES DEPRESSED DURING THIRD QUARTER
AS FINANCIAL PRESSURES ON GOP INTENSIFY

REF: PANAMA 7225

1. SUMMARY: THE ECONOMY CONTINUED AT A SLOW PACE DURING THE 1976 THIRD QUARTER, BUT DID NOT DETERIORATE FURTHER FROM THE DEPRESSED SECOND QUARTER LEVEL. GOVERNMENT REVENUES AGAIN FAILED TO REACH BUDGETED LEVELS, CURBING OUTLAYS AND FORCING ADDITIONAL LOAN DIVERSION AND ACCOUNT MANIPULATION IN ORDER TO MEET CURRENT OBLIGATIONS. THERE IS NO SIGN OF IMMINENT STRENGTHENING IN EITHER THE ECONOMIC OR FINANCIAL SITUATION. A PRESSING PROBLEM THE GOP NOW FACES IN THIS AREA IS ARRANGING A SYNDICATED FOREIGN BANK CREDIT OF \$100 MILLION OR MORE WHICH THE GOP NEEDS IN ORDER TO REMAIN SOLVENT AND MAINTAIN ITS CURRENT LEVEL OF OPERATION. THIS EFFORT IS CURRENTLY UNDERWAY. FINANCIAL AND ECONOMIC PRESSURES APPEAR
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SUFFICIENT TO ACCOUNT FOR GOP URGENCY IN SEEKING AGREEMENT ON A NEW TREATY FAIRLY EARLY IN 1977. END SUMMARY.

2. SLOW ECONOMIC PACE CONTINUES THROUGH THIRD QUARTER
PANAMA'S ECONOMY DURING THE 1976 THIRD QUARTER WAS
LITTLE CHANGED FROM THE DEPRESSED SECOND QUARTER LEVEL.

WHILE HOPES FOR SIGNIFICANT IMPROVEMENT IN SUCH HARD HIT SECTORS AS CONSTRUCTION WERE NOT FULLY REALIZED, AT LEAST THE SHARP SECOND QUARTER DECLINES APPEAR TO HAVE BEEN ARRESTED. MANUFACTURING WAS DOWN SLIGHTLY. THE VALUE OF CONSTRUCTION PERMITS REMAINED LOW BUT WAS SOMEWHAT IMPROVED OVER THE EXTREMELY DEPRESSED SECOND QUARTER LEVEL. UNEMPLOYMENT WAS OFFICIALLY REPORTED DOWN SLIGHTLY TO 6.5 PERCENT ALTHOUGH THE TRUE LEVEL IS GENERALLY THOUGHT TO BE MUCH HIGHER AND THE PROBLEM MORE SERIOUS THAN OFFICIAL FIGURES INDICATE. DOMESTIC BANK LENDING INCREASED SEASONALLY TO ABOUT THE YEAR AGO LEVEL. WHOLESALE AND RETAIL PRICE INDEXES STEADIED AT 6.5 PERCENT AND 3 PERCENT RESPECTIVELY ABOVE A YEAR AGO, ALTHOUGH INFLATION IS ESTIMATED TO HAVE BEEN FAR MORE PRONOUNCED THAN THESE INDEXES INDICATE. THE BALANCE OF PAYMENTS ALSO REMAINED WEAK. EXPORTS DECLINED GENERALLY IN THE THIRD QUARTER, WHILE IMPORTS OF CONSUMPTION AND INTERMEDIATE GOODS INCREASED, DUE IN PART TO INCREASED PETROLEUM PRODUCTS IMPORTS STEMMING FROM THE REFINERY SHUTDOWN EARLIER IN THE YEAR. CAPITAL GOODS IMPORTS REMAIN CONSIDERABLY BELOW LAST YEAR'S LEVEL. TOURISM RECEIPTS CONTINUED TO DECLINE DURING THE THIRD QUARTER; TRANSACTIONS WITH THE CANAL ZONE WERE LITTLE CHANGED. FOR THE FIRST NINE MONTHS TOURISM WAS DOWN 12 PERCENT AND CANAL ZONE TRANSACTIONS DOWN 9 PERCENT FROM THE CORRESPONDING 1975 PERIOD.

3. GOP REVENUES AND EXPENDITURES REMAIN BELOW BUDGET REVENUES FOR NINE MONTHS TOTALLED \$210 MILLION (\$205 MILLION IN 1975), ABOUT \$20 MILLION BELOW BUDGET. CURRENT EXPENDITURES WERE DOWN SOMEWHAT LESS, HOWEVER, SINCE \$25-30
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MILLION IN BORROWED FUNDS HAVE BEEN DIVERTED SO FAR THIS YEAR TO COVER CURRENT EXPENSES. CAPITAL OUTLAYS TO DATE (BASICALLY FOREIGN FINANCED) ARE ABOUT THE SAME AS IN 1975 FOR THE CENTRAL GOVERNMENT. DATA ON CAPITAL OUTLAYS AND DEBT SERVICING BY THE AUTONOMOUS AGENCIES ARE INCOMPLETE, ALTHOUGH CAPITAL SPENDING PROBABLY HAS BEEN SUBSTANTIALLY LESS THAN BUDGETED IN VIEW OF THE FINANCIAL STRAINS BEING EXPERIENCED THROUGHOUT GOVERNMENT.

4. SHORT TERM OUTLOOK BLEAK

(A) THIRD QUARTER CHANGES IN THE ECONOMY FAILED TO SIGNAL ANY SIGNIFICANT IMPROVEMENT IN PANAM'S SHORT TERM ECONOMIC PROSPECTS. WHILE THE GENERAL DECLINE APPEARS TO BE ARRESTED, CURRENT SLUGGISHNESS IS LIKELY TO CONTINUE SINCE THERE IS NO FIRM EVIDENCE OF ANY EARLY UPTURN IN PRIVATE INVESTMENT. A COMPLICATING FACTOR IS THE GOP'S PRESSING NEED TO BOLSTER ITS FINANCIAL POSITION THROUGH

EXPENDITURE CURBS AND INCREASED TAXES. SUCH MEASURES WOULD RUN COUNTER TO THE ECONOMY'S SHORT RUN NEEDS AND WOULD FURTHER RESTRICT THE GOP'S CAPACITY TO SUSTAIN ITS INVESTMENT PROGRAM WHICH IS NEEDED TO HELP OFFSET THE PRESENT DEARTH OF PRIVATE INVESTMENT.

(B) THE GOP'S SHORT RUN FINANCIAL OUTLOOK POSES A MORE IMMEDIATE THREAT TO PANAMA'S FINANCIAL AND ECONOMIC STABILITY THAN DOES RECESSION. PRESSURE ON GOP LIQUIDITY HAS BECOME INTENSE. THERE ARE A FEW KNOWN (AND NUMEROUS REPORTED) INSTANCES OF GOP DEPARTMENTS AND AGENCIES MANIPULATING ACCOUNTS TO MEET CURRENT OBLIGATIONS, EVEN PAYROLLS. WE SEE NO INDICATION OF EARLY RELIEF. THE EXISTING REVENUE STRUCTURE CANNOT BE EXPECTED TO YIELD MORE IN 1977 THAN THE LESS-THAN-BUDGETED LEVELS OF 1976. RECENT PUBLIC STATEMENTS REGARDING THE NEED FOR HIGHER TAXATION STILL HAVE NOT RESULTED IN A SPECIFIC TAX PROPOSAL, ALTHOUGH VARIOUS COMBINATIONS
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YIELDING \$20-30 MILLION ANNUALLY (MOSTLY IN NEW CONSUMER TAXATION) HAVE BEEN CONSIDERED. EVEN IF A SPECIFIC PACKAGE WERE TO BE AGREED UPON SOON, THERE WOULD BE A LAG OF SOME MONTHS BEFORE FULL IMPLEMENTATION AND RESULTANT FISCAL BENEFITS WOULD BE FELT. WHILE THE OPERATING BUDGET FOR 1977 IS EXPECTED TO BE AUSTERE, IT WILL STILL NEED TO PROVIDE FOR CERTAIN BUILT-IN INCREASES SUCH AS DEBT-SERVICING--A MINIMUM OVERALL INCREASE OF AROUND \$30 MILLION ABOVE THE 1976 "ACTUAL" IS THE LATEST OF SEVERAL ESTIMATES OF ESSENTIAL INCREASE CITED BY SENIOR GOP OFFICIALS. THERE IS LITTLE POSSIBILITY OF A CURRENT ACCOUNT SURPLUS IN 1977 FROM EITHER THE CENTRAL GOVERNMENT OR ITS AGENCIES, AND THE PUBLIC SECTOR INVESTMENT PROGRAM, ALTHOUGH FINANCED LARGELY BY INTERNATIONAL FINANCIAL INSTITUTIONS, STILL REQUIRES A SIZEABLE GOP INPUT. HENCE, AN EARLY LARGE INJECTION OF NEW RELATIVELY FLEXIBLE CREDIT FROM PRIVATE FOREIGN BANK (OR NON-TRADITIONAL, E.G., ARAB) SOURCES SEEMS ESSENTIAL IF THE GOP IS TO SURVIVE A DEVELOPING LIQUIDITY CRISIS AND SUSTAIN ITS PRESENT SOMEWHAT CURTAILED INVESTMENT PACE.

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C O N F I D E N T I A L SECTION 2 OF 2 PANAMA 8521

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(C) PRELIMINARY DISCUSSIONS REGARDING A POSSIBLE SYNDI-
CATED CREDIT IN THE \$100 MILLION PLUS RANGE ARE REPORTEDLY
UNDERWAY BETWEEN GOP OFFICIALS AND REPRESENTATIVES OF
PANAMA'S INTERNATIONAL BANKING COMMUNITY. A DETERMINED
EFFORT TO PUT TOGETHER SUCH A PACKAGE IS EXPECTED IN
VIEW OF THE SUBSTANTIAL STAKES MAJOR U.S. AND OTHER FOREIGN
BANKS HERE HAVE IN PANAMA. THIS IS THE MINIMUM WE CONSIDER
ESSENTIAL TO AVERT A MAJOR FISCAL CRISIS, I.E., A VISIBLE
WAVE OF GOP DEFAULTS ON CURRENT OBLIGATIONS INCLUDING
DEBT SERVICING. HOWEVER, A LOAN OF THIS SIZE WILL BE MORE
DIFFICULT TO SYNDICATE AND WILL HAVE STRICTER CONDITIONS
IMPOSED THAN SIMILAR FINANCING OBTAINED EARLY IN 1976.
THERE IS NO ASSURANCE OF SUCCESS IN THIS EFFORT AND A
PACKAGE MUCH BELOW \$100 MILLION MIGHT WELL CONSTITUTE
FAILURE. ALSO OF SIGNIFICANCE, THE PROCESS WILL BE
WATCHED CLOSELY BY OTHER LESSER BUT NONETHELESS ESSENTIAL
POTENTIAL CREDITORS STANDING IN THE WINGS, EYEING ANY
SIGN OF DIFFICULTY THAT MIGHT TURN OFF THEIR INTEREST
IN ADDITIONAL LENDING TO PANAMA. ONE ENCOURAGING FACTOR
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IS THAT THERE MAY BE POTENTIAL INTERNATIONAL CREDITORS
NEW TO THE PANAMANIAN SCENE WILLING TO PARTICIPATE IN
ORDER, FOR EXAMPLE, TO DIVERSIFY THEIR PORTFOLIOS GEO-
GRAPHICALLY. ON THE OTHER HAND, REPEATED REFERENCES TO
LARGE ARAB LOANS TO PANAMA NEVER SEEM TO GO BEYOND THE
RUMOR STAGE.

(D) IN VIEW OF THE FOREGOING, THE GOP IS VERY LIKELY
TO PRESS FOR A MAJOR DEBT RESCHEDULING IN 1977,

INVOLVING PRIMARILY HOLDERS OF PANAMA'S SHORT AND MEDIUM TERM DEBT.

5. COMMENT: THE PANAMANIAN GOVERNMENT HAS FEW MEANS FOR EXTRICATING ITSELF FROM ITS ECONOMIC AND FINANCIAL DILEMMAS. PANAMA IS NOW VIRTUALLY AT THE MERCY OF A HANDFUL OF PRIVATE INTERNATIONAL BANKERS IN TERMS OF THE FISCAL SITUATION AND OF A HANDFUL OF PRIVATE INVESTORS IN TERMS OF THE ECONOMY. AS A RESULT, PANAMANIAN OFFICIALS ARE BECOMING FEVERISH IN THEIR PURSUIT OF AN EARLY TREATY SETTLEMENT, HOPING THAT IT WILL RELIEVE THEIR ECONOMIC AND FINANCIAL WOES. (THE EMBASSY BELIEVES THAT A TREATY SETTLEMENT BY ITSELF WILL NOT SOLVE PANAMA'S PROBLEMS, BUT THAT A TREATY ACCEPTABLE TO PANAMA IS ESSENTIAL TO ECONOMIC RECOVERY AND TO MAINTAINING PANAMA'S BORROWING CAPACITY.) PANAMANIAN OFFICIALS SEEM INCREASINGLY MOTIVATED BY A FEAR THAT, WITHOUT A TREATY, TIME COULD RUN OUT IN 1977--PERHAPS BY SUMMER--I.E., A SEVERE FINANCIAL CRISIS COULD OCCUR, BRINGING ON SERIOUS POLITICAL PROBLEMS. THE FOREIGN MINISTER'S TWO-WEEK VISIT TO THE U.S. WAS AIMED PRIMARILY AT AVOIDING UNDUE DELAY BECAUSE OF THE U.S. TRANSITION. HIS BRAVE TALK OF INTENSIVE WORK ON THE TREATY IN THE NEXT THREE MONTHS (PANAMA 8444) IS FURTHER EVIDENCE OF A GOP REALIZATION THAT IT HAS NO TIME TO LOSE.

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